

A Novel Approach to Construction Disputes: An Overview of Dispute Adjudication Boards

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Introduction

Due to the nature and volume of disputes which arise in a construction context, the construction industry has been a forerunner in implementing measures to avoid and, as is often necessary, manage disputes. Traditionally, contracting parties would use either litigation or alternative dispute resolution procedures (such as arbitration or mediation) to resolve construction disputes. In recent years, there has been a shift in the way parties approach and manage disputes, with some parties seeking to implement preventative processes at the outset of a contract to assist in avoiding and managing potential disputes.

The use of a dispute adjudication board (DAB) is one approach which may assist parties in avoiding and proactively managing disputes. The use of a DAB is a proactive, rather than a reactive, approach for parties to take to dispute resolution. Rather than engaging in a dispute resolution procedure once a dispute has arisen, using a DAB assists in avoiding potential disputes² and to ensure that unavoidable disputes can be resolved in an efficient, cost-effective manner. This paper discusses the process adopted by DABs in resolving disputes, various factors which can help or hinder the effectiveness of a DAB and the benefits and cost implications for parties of using a DAB. For parties seeking to proactively manage disputes, DABs are a very attractive option.

Use of a DAB

Any commercial party entering into a construction contract should consider using a DAB. Setting up a board which will be intimately acquainted with the parties' contract and project and which can then step in to resolve disputes in 'real time' is a proactive way to manage disputes.

Although there has been limited use of DABs in Australia, the concept of a DAB first appeared in the International Federation of Consulting Engineers (FIDIC) Design and Build Contract in 1995.³ A DAB operates in a similar fashion to a dispute resolution board (DRB); however, the DAB procedure is more formal and structured than the DRB procedure and the DAB's decision is binding on the parties.

Because a DAB entails a dispute avoidance procedure, as opposed to a dispute resolution procedure, a DAB is generally provided for in the construction contract and set up at the outset of a project to assist the parties with managing and resolving disputes which may arise.

1 BA, LLB, University of Western Australia, Solicitor, Mallesons Stephen Jaques.

2 Paula Gerber, 'The Changing Face of Construction Dispute Resolution in the International Arena: Where to From Here?' (2000) 73 Australian Construction Law Newsletter 5.

3 Sally Kirby, 'Do "dispute boards" offer any solutions to the challenges faced by traditional forms of dispute resolution in the Australian construction industry?' (2008) 20(6) Australian Construction Law Bulletin 56, 58.

The DAB is constituted of a board of either one or three members. FIDIC suggests that if the contract price exceeds US \$25 million, the board should be constituted by three members. If the parties choose to have a three-member board, typically, each party will choose one member (for approval by the other party). The third member should be mutually agreed upon.⁴ If the parties opt for a one-member board, the parties should mutually choose that member.⁵ It is critical that the members of the DAB remain independent throughout the contracting period.

Once the DAB has been appointed by the parties, it should:

- 1 be provided with copies of the contract documents and (as they are rendered) progress claims, payment certificates, variation claims, extension of time claims;
- 2 request copies of any further documents (such as site meeting minutes, contract meeting minutes, reports of the independent certifier and so on) that it may require;⁶
- 3 be regularly informed about the progress of the works; and
- 4 visit the site regularly, or at the very least 'at the times of critical construction events'⁷ and no less than three times per year.

This allows the DAB to be fully informed of both the construction's progress and the claims being made. The benefits of this are discussed below.

If a dispute arises that the parties are unable to resolve amongst themselves, the referral of the dispute to the DAB and the resolution of the dispute by that board is a somewhat formal and structured process. To invoke the DAB's power to resolve the dispute, there must in the first instance be a relevant 'dispute' for referral to the DAB.⁸ Provided there is such a 'dispute', and one of the parties (in writing) refers it to the DAB, there is a specific procedure to be followed by the DAB.

The DAB will:⁹

- 1 call for submissions from the (non-referring) party;
- 2 conduct a hearing; and
- 3 give its decision to the parties within a defined (short) period of time¹⁰ of the dispute being referred.

DAB decisions are immediately binding upon the parties and will become final if there is no notice of dissatisfaction issued within 28 days of the decision.¹¹ If one party issues a notice of dissatisfaction, the parties then have limited time¹² within which to attempt to settle the matter amicably. If the matter

4 Christopher Seppala, 'The New FIDIC Provision for a Dispute Adjudication Board' (1997) 8 *International Construction Law Review* 967, 969.

5 *Ibid.*

6 *Ibid.* 970.

7 *Ibid.*

8 See also Seppala, above n 5.

9 See Seppala, above n 5.

10 Under FIDIC contracts, this time period is 84 days.

11 Robert M Mayes et al, *Construction Dispute Review Board Manual* (1996) cl 1.3.1; International Federation of Consulting Engineers (FIDIC), *Conditions of Contract for Construction and Building for Building and Engineering Works Designed by the Employer* (1st ed, 1999) Appendix: General Conditions of Dispute Adjudication Agreement cl 20.4 (FIDIC Red Book).

12 Under the FIDIC contracts, this time period is 56 days.

13 Above n 12, FIDIC Red Book, clause 20.6.

cannot be settled, commonly, it can be finally resolved by arbitration. It is notable that a decision of the DAB will generally be admissible as evidence in any subsequent arbitration proceedings.¹³

It has been suggested that DABs are only suited to larger projects where the value of the contract exceeds \$30 million.¹⁴ However, all parties can and should consider using a DAB, even in the context of a small project. In smaller projects it may be more appropriate to appoint a single board member, as opposed to three members, in order to keep the cost of the DAB proportionate to the contract value. In the author's opinion, a DAB can be successfully used on both large and smaller-scale projects.

Effectiveness of a DAB

Due to its ongoing involvement in major projects and the speed with which it is able to resolve disputes, a DAB can assist parties to successfully avoid and/or manage construction disputes. There are several factors which may enhance or reduce the effectiveness of a DAB. These factors include, but are not limited to:

- 1 the appropriate selection of board members;
- 2 the parties' willingness to participate in and embrace the DAB process; and
- 3 the parties' willingness to accept the decision(s) of the DAB.

The selection of DAB members is arguably one of the most critical factors in establishing an effective DAB. The parties need to carefully consider the appropriateness of potential DAB members. Often, the board will be (and should be) comprised of either engineers, quantity surveyors or project managers who have experience with similar projects and generally the chair of the board may be a lawyer.¹⁵ The parties should research each person thoroughly and ensure that they have the appropriate background to assist in resolving the disputes that may arise during the project. One 'bad egg' amongst the board members may hinder the effectiveness of the DAB, whereas three competent, highly-skilled individuals with prior experience on similar projects will greatly assist its effectiveness.

The parties' willingness to submit to DAB processes will impact the success of a DAB. Once a DAB is appointed, the parties must work with it for the duration of the contract. It is almost worthless to appoint a DAB if the parties are not prepared to properly engage in the dispute adjudication process outlined in the contract. Further, a level of transparency is required of the parties and it is necessary that they be upfront with one another and discuss any potential disputes. If the parties are not willing to be proactive in the avoidance and management of disputes and are not willing to engage in the process, the DAB will not be able to fulfil its role effectively.

The effectiveness of a DAB will also be affected by the parties' willingness to accept the DAB's decision(s). Aggrieved parties may choose to refer the dispute to arbitration if dissatisfied with the DAB's decision. However, such an adversarial approach renders the DAB less effective. Alternatively, if parties are prepared to accept the 'swings and roundabouts' of DAB decisions, their DAB will be more effective and both the project and parties are likely to benefit.

14 See Donald Charrett, 'Dispute Boards and Construction Contracts' (2010) 132 Australian Construction Law Newsletter 18, 18.

15 Above n 4.

16 Dispute Resolution Board Foundation, DRBF Practices and Procedures Manual (2007) cl 1.3 <

Benefits of a DAB

There are a number of benefits which flow from the appointment of a DAB. Broadly, using a DAB assists in:

- 1 preventing disputes;
- 2 encouraging open communication between the parties; and
- 3 resolving disputes expediently and (usually) without any need for the parties to look to costly arbitration or litigation processes.

Having a DAB in place is said to facilitate ‘positive relations, open communication, and the trust and cooperation that is necessary for the parties to resolve problems amicably’.¹⁶ As a result of the structure of the DAB and the regular onsite meetings the process entails, the parties are able to focus on identifying and resolving disputes at an early stage in the contracting process. Having a DAB in place may also encourage parties to negotiate and resolve disputes ‘at job level’ before referral to the DAB.¹⁷ This is often because, having themselves constituted the DAB, parties have respect for and confidence in its members.¹⁸ As a result, parties do not want to be seen to be pursuing trivial disputes.¹⁹ Quite often, disputes are resolved without resorting to the DAB’s intervention. George Golvan makes the point that ‘[o]f the twenty or so projects using dispute resolution boards in Australasia ... very few disputes are known to have been referred to dispute resolution boards for recommendation or determination ...’.²⁰

When parties are unable to resolve a dispute themselves, they are able to refer it to the DAB, which will generally understand the project and have a thorough knowledge of the contract documents. This allows DAB members to step in and offer ‘quick, well-informed, even-handed and consistent responses’.²¹ As the board members have such an intimate knowledge of the project, are kept abreast of developments, have first-hand knowledge of the facts²² and are able to hear the dispute just after it has occurred, they are able to quickly produce well-informed decisions when resolving disputes.

From the contractor’s perspective, the inclusion of a DAB clause into the contract is a strong instrument to enforce interim claims against the principal. To the extent that the contractor has a claim to make, it can refer the claim as a ‘dispute’ to the board, which will then resolve it and issue its decision, which is binding on the parties. This is a significant benefit for contractors, who are often plagued by issues of non-payment and cash flow.

http://www.drb.org/manual_access.htm at 20 November 2010.

17 Dispute Resolution Board Foundation (Australasian Chapter), Dispute Resolution Board Concept <<http://www.drb.org/concepts.htm>> at 20 November 2010.

18 Above n 2, 27.

19 Above n 4.

20 George Golvan, ‘Practical Issues in the Establishment and Operation of a Dispute Resolution Board – Some Reflections on Sydney’s Desalination Plant Project Dispute Resolution Board’ (2010) 132 Australian Construction Law Newsletter 30, 31.

21 Graeme Peck and Peer Dalland, ‘The Benefits of Dispute Resolution Boards for Issue Management of Medium to Large Construction Projects’ (2007) 26(1) Arbitrator & Mediator 13, 19.

22 Dispute Resolution Board Foundation (Australasian Chapter), above n 17.

23 Ibid.

Given that a DAB deals with and resolves disputes as they arise, one of the additional benefits from the perspective of a principal is the avoidance of ‘end of contract claims’.²³ That is, avoiding the ability of contractors to bundle all their claims (for variations, extensions of time and so forth) at the end of the contract, thereby taking the principal by surprise. The fact that the DAB is able to step in and resolve disputes as they occur allows the principal to more closely control its budget and (in most cases) avoid the costs of unpredictable arbitration or litigation which may occur after completion of the project.²⁴

One of the aims of using a DAB is to avoid arbitration or litigation proceedings. Some parties, however, still like the idea of their ‘day in court’. The DAB provides parties with the opportunity to present their cases in an impartial forum and have their day in court,²⁵ without the need to actually commence proceedings. The flow-on benefit is that the parties avoid the legal and/or consultants’ costs that would otherwise be incurred were the disputes referred to arbitration or litigated.

Despite its many advantages, there remain some disadvantages to using a DAB. These include the cost of running a DAB (discussed below) and the fact a DAB may not be suitable for all contracts. To use a DAB on a small-scale construction project, although possible, may not be cost-effective in the long run. Some also argue that DAB decisions are ‘rough and ready’ as a result of the short period of time the board members have to prepare their decision(s). However, given that no disputes which arise in contracts that use dispute boards have been referred to arbitration or litigated, in the author’s view this concern does not appear to be of significance.

The Cost of a DAB

A potential downside to using a DAB is the cost involved. Implementation of a DAB can be expensive and constitutes a direct cost, one not ordinarily built into construction contracts. The cost of implementing a DAB is said to be between 0.15% and 0.26% of the total project cost.²⁶ In some instances, however, the costs are reported to be as high as 1% of the contract.²⁷ This cost of the DAB is shared equally between the parties. The actual cost to the parties of a DAB will depend on factors such as the duration of construction, the number of disputes referred to the DAB and the complexity of those disputes.²⁸

The costs involved in implementing and using a DAB arise from the remuneration of board members. Remuneration should be mutually agreed upon by the parties and the members. It has been suggested that if the parties are unable to agree, then DAB members’ remuneration should include:

- 1 a fixed daily fee, for each day the members work;

24 Ibid.

25 Gerber, above n 2, 27.

26 Ibid 26.

27 Gwen Owen, Introduction to FIDIC Dispute Adjudication Board Provisions: Conditions of Contract for Construction – FIDIC 1999 <<http://www.scribd.com/doc/17735312/Introduction-to-FIDIC-Dispute-Adjudication-Board-Provisions-Owen2004>> at 21 November 2011.

28 Paula Gerber, ‘Construction Dispute Review Boards’ (1999) 10 Australian Dispute Resolution Journal 9, 12.

29 Seppala, above n 5, 970.

- 2 a retainer fee (per month) to ensure the members' continued availability, equivalent to three times the daily fee; and
- 3 reimbursement for reasonable expenses.²⁹

These costs are significant and the parties will have to incur them regardless of whether a dispute in fact arises. It may be that no disputes arise during the course of construction and so in this case the cost of the DAB would outweigh the benefit it may provide. Realistically, though, in all major construction projects there is likely to be at least one dispute between the parties. Parties need to consider the costs incurred in using a DAB during the term of a contract, in contrast to the potential cost saving in the event that no disputes are referred to arbitration or litigated.³⁰ When compared with the costs that parties could potentially incur in the event of a dispute which did proceed to arbitration or was litigated (estimated to be between 8% and 10% of the total project cost),³¹ a DAB is an effective way to manage disputes. The cost of implementing a DAB should be looked at by the parties as an 'insurance cost', paid to reduce the risk of the parties having to engage in costly arbitration or litigation.³²

One further consideration for parties is the cost saving which results from the reduction in loss of productive project time. Because disputes are dealt with as they arise and DAB board members have a working knowledge of the project, the dispute can be dealt with and resolved quickly, reducing the loss of productive time.³³

Conclusion

The use of a DAB in construction contracts is a welcome shift in the traditional approach parties have taken to construction disputes. Using a DAB is a proactive, rather than a reactive, approach to dispute resolution. Gerber describes dispute avoidance procedures, which include DABs, as being the 'legal equivalent of preventative medicine'.³⁴ It is far better to attempt to prevent disputes at the front end of a project, through mechanisms such as DABs, rather than having to engage in costly and time-consuming litigation or arbitration at the back end. The benefits to the parties are immense. Not only should they be better able to communicate with each other as a result of having used a DAB, but they will have three very qualified members, whom they have chosen and trust, on hand to resolve their disputes in a timely manner.

Although parties are required to outlay money upfront to remunerate members of the DAB, this should result in a cost saving to the parties as a result of there being less productive time lost and minimal possibilities of either arbitration or litigation during the life of the project. Of course, the success of the DAB in preventing disputes will largely be determined by the parties themselves and how responsive

30 George Golvan notes that of the 20 or so contracts which have used dispute boards in Australian, none have led to litigation. See above n 20, 31.

31 Gerber, above n 2, 26.

32 Ibid 25.

33 Ibid 27.

34 Paula Gerber, 'Dispute Avoidance Procedures ("DAPs") – The Changing Face of Construction Dispute Management' (2001) 18(1) International Construction Law Review 122, 129.

they are to the process, the way in which they communicate with each other and with the DAB. Whilst a DAB is not the sole solution to avoiding and managing construction disputes, it is one viable option worthy of consideration by parties to construction contracts and contract drafters.

